Retail Drug

MEMORANDUM FOR OFFICE USE ONLY

E. S. WARNER
1840 UNION COMMERCE BLDG.
CLEVELAND, OHIO

UNITED DRUG COMPANY

$20,000,000 Sinking Fund 3 1/4% Debentures - August 1, 1958.

$10,000,000 Cumulative 4 3/4% Preferred Stock, (Par $100)

United Drug Company, successor to a business established 1902, is an operating and holding company engaged directly and through subsidiaries in -

(a) Manufacturing and distributing drugs, pharmaceuticals, proprietaries, toilet articles, stationery, food and chocolate products, rubber articles and other products used in or sold by drug stores.

(b) The operation, through subsidiaries, of retail drug stores.

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MANUFACTURE AND DISTRIBUTION

United Drug Company manufactures or processes approximately 2,400 different products which include a practically complete line of drugs, pharmaceutical, medicinal products and cosmetics, which are sold under many brand names. Best known are Rexall, Puretest, Plenamins, Multamins, Bisma-Rex, Mi-31, Cara Nome, Adirenne, Klenzo, Stag, and Briten. Many products are made for the general drug trade often under private brand-names, as, for example, drugs for Sears Roebuck & Company.
The Seamless Rubber Company manufactures water bottles, syringes of many types, bath sprays, rubber gloves, adhesive plaster and tape, rubber bands, nipples, combs, bathing suits and caps, bladders, play balls and rubber toys. (At present engaged in war work).
United Drug Company, Ltd. (Canada) manufactures medicines, pharmaceuticals, toilet goods and cosmetics in Toronto, Ont.
Hudson Valley Pure Food Company, Inc. makes grape juices, soda fountain fruits, chocolate and other syrups, preserves, jellies and other food products, a large percentage of which is sold outside the Rexall group.
United Chocolate Refiner, Inc. makes chocolate, cocoa, coatings, chocolate bars, candy, and similar products, much of which is sold to the general trade.
United Tablet Corp. manufactures stationery, writing tablets, envelopes, paper drinking cups, and other related products.
The Absorbent Cotton Company) Manufacture absorbent cotton, gauzes, bandages,
United Cotton Products Company) dressings and allied products.

The distribution by the Company throughout the U. S. and Canada of the above products. The products manufactured by the Company, and various products which are manufactured for it by others are not sold on the open market generally, but are distributed to selected dealers under private labels. The selected dealers of which there are 8,217 in the United States and 1,061 in Canada are designated "The Rexall Drug Store." These Rexall Stores are owned and operated by independent dealers who have contracts with the Company giving them an exclusive franchise in their area for the sale of products manufactured or distributed by the Company. These Rexall Stores constitute the major outlet for the Company's private-labeled products although such products are also sold through the Company's owned and operated stores.

RETAIL OPERATIONS

The Company operates, through subsidiaries, 568 retail drug stores-

(1) Liggett Drug Company, Inc. operates 387 drug stores in 207 cities in the U. S. east of the Rockies.
(2) The Owl Drug Company operates 134 stores in 35 cities principally on the West Coast. (U.S.)
(3) Louis K. Liggett Company, Ltd. (Canada) operates 47 stores in 19 cities in Canada.

The Company during the past three years has consolidated and coordinated many of its facilities and operations, resulting in greater efficiency and economy. The leasing policy of the retail group has undergone a material change in the past two years, so that, in general, new leases and renewals are being taken with cancellation privileges and rentals based on earnings. The present objective is to eliminate unprofitable small volume stores, to modernize existing stores, and to develop so-called supertype stores in metropolitan centers, several of which are now in operation. During the past five years 90 stores were closed and 37 added, a net decrease of 53 stores for the period. Since 1933 it has been the policy of the Company not to assume or guarantee any leases of its subsidiaries.

In 1942 Mr. Justin W. Dart was elected president of the Company's major retail subsidiary, Liggett Drug Company, Inc., and in April 1943 he was elected president of the Company's parent, United Drug, Inc. Prior to his association with the Company, Mr. Dart was with Walgreen Co., having been in charge of the operations of that company's retail stores from 1932 to 1939, and its general manager from 1939 until his resignation in October, 1941. It is anticipated that many of the merchandising methods and operating policies which Mr. Dart inaugurated successfully in that company will be applied to the operations of the retail stores of this Company's subsidiaries.

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The relative contributions for the past six calendar years of the Company's manufacturing operations and its retail subsidiaries to Consolidated Net Sales and to Consolidated Profits are shown by the following figures:

	Manufacturing Group		Retail Group		
	Sales	%	Sales	%	Total
1937	$26,457,920	28.34	$66,900,338	71.66	$ 93,358,258
1938	24,552,745	27.94	63,314,483	72.06	87,867,228
1939	25,513,580	28.55	63,842,801	71.45	89,356,381
1940	25,834,601	28.61	64,463,531	71.39	90,298,132
1941	31,754,767	30.99	70,706,193	69.01	102,460,960
1942	38,821,622	31.82	83,176,355	68.18	121,997,977
	Profits	%	Profits	%	
1937	$ 3,002,802	74.06	$ 1,051,754	25.94	$ 4,054,556
1938	2,610,104	88.03	354,912	11.97	2,965,016
1939	3,244,967	87.93	445,549	12.07	3,690,516
1940	3,177,398	84.01	604,567	15.99	3,781,965
1941	4,566,135	69.52	2,002,026	30.48	6,568,161
1942	6,433,961	56.52	4,950,404	43.48	11,384,365

Note-Consolidated Profits shown above are before deducting interest charges, guaranteed lease losses and charges, provisions for taxes on income, provisions for contingencies and for possible future losses and adjustments.

	Loss from operation of guaranteed leases.	Provisions for contingencies and for possible future losses.	Available for interest and income taxes
1937	$ 391,334	$ --	$ 3,663,222
1938	434,504	--	2,530,512
1939	464,367	83,389	3,142,760
1940	468,230	50,000	3,263,735
1941	413,936	300,000	5,854,225
1942	1,444,504*	800,000	9,139,861
1943 (5 Mo.)	71,458	235,000	4,820,823

*Includes $1,160,546 for cancellation or modification of certain guaranteed leases. These payments and the expiration in June 1943 and in April 1944 of two of these leases will reduce substantially the annual lease losses. There remain three guaranteed leases on which there was a loss to the Company of $130,042 in 1942, and a loss of $68,462 in the first five months of 1943.

Such earnings, assuming interest at 3¼% on $20,000,000 of Debentures and 4¾% rate on $10,000,000 Preferred Stock, would cover such requirements as follows:

	INTEREST		PFD. DIV.	OVERALL
	Before Income Taxes	After Income Taxes	After Taxes	After Taxes
1937	5.64	4.42	4.69	2.56
1938	3.89	3.07	2.83	1.77
1939	4.84	3.97	4.06	2.29
1940	5.10	4.01	4.12	2.32
1941	9.47	6.60	7.66	3.81
1942	15.29	6.33	7.30	3.66
1943 (5 Mo.)	18.67	6.20	7.11	3.58

	Per $1,000 Debenture	Per Share Preferred
Net Tangible Assets.....$47,245,000	$2,362	$272
Net Current Assets..... 30,581,000	1,529	104

July 30, 1943

SALESMEN'S CONFIDENTIAL MEMORANDUM:

TWO ATTRACTIVE INCOME ISSUES
UNITED DRUG COMPANY S. F. DEBENTURE 5 1/4s*, 1958 and 4 3/4%* PREFERRED

One of the leading units in the drug manufacturing and distribution field, this Company occupies an important position in an essential and growing industry. With a new management which already has realigned executive personnel and brought about higher operating efficiency and with its capital structure to be materially improved by the proposed financing, the Company faces what we believe to be a period of continued sales and earnings betterment. Output currently is at record levels and the post-war era seems to hold a good deal of promise. Thus, its new securities which will be offered on attractive yield bases should be suitable for many types of investors interested primarily in income.

The new Debentures will be well secured, in our opinion, both by net current and net fixed assets as well as by a wide margin of earnings. They will enjoy the benefits of a Sinking Fund, furthermore, which is designed to retire approximately 50% of the issue by maturity. So far as the Preferred stock is concerned, it, too, will enjoy satisfactory earnings and assets protection and will compare favorably with other issues of similar investment quality. The Debentures, it is expected, will be eligible for purchase by national banks and the Preferred stock should be appropriate for private investors.

THE COMPANY: Business of United Drug Company is divided into the two inter-related divisions of manufacture and distribution of drugs, medicines and other preparations usually sold in drug stores. United Drug Company itself is both a holding as well as a manufacturing concern; its subsidiaries, in turn, produce and distribute their own as well as the products of other manufacturers. All of the Common stock of United Drug Company is owned by United Drug, Inc., the holding company. Stock of this latter concern is the one which is listed and actively traded on the New York Stock Exchange.

Outgrowth of a business originally organized in 1902, the present United Drug Company is one of the largest factors in its industry. In its plants at Boston and St. Louis, it manufactures or processes approximately 2,400 different products which include a practically complete line of drugs, pharmaceuticals, medicinal products and cosmetics. These are sold under many brand names, among the best known of which are "Rexall", "Puretest", "Bisma-Rex" and "Cara Nome". Supplementing these products are a wide range of rubber goods, grape juice and soda fountain fruits, candies, stationery, cotton gauze and bandages and many others.

All of these products as well as similar lines manufactured for the Company by others under its private labels are distributed generally to selected dealers throughout the United States and Canada who constitute the major outlet for such products. The selected dealers, of which there are approximately 8,000 in the United States and 1,000 in Canada are known as "Rexallites" and each of their stores is designated as "The Rexall Drug Store". All are owned and operated by independent dealers under contracts with the Company which gives them an exclusive franchise in their respective territories for the sale of its merchandise. Supplementing these units, however, are the more than 500 retail drug stores of Liggett Drug Company, Inc. and The Owl Drug Co., subsidiaries. These are also designated as "Rexall Drug Stores" and serve on practically the same terms as the "Rexall" dealers.

CAPITALIZATION: Proceeds from sale of the new issues together with such Company funds as may be required will be used to retire the $50,243,200 principal amount of Debenture 5s due 1953 currently outstanding. Upon completion of the financing, therefore, capitalization will be as follows:

Issue	Authorized	Outstanding
Debenture S.F. 5 1/4s*, 1958	$20,000,000	$20,000,000
4 3/4%* Preferred ($100 par)	100,000 shs.	100,000 shs.
Common Stock ($50 par)	140,056 "	140,056ϕ "

* Assumed rate. ϕ All owned by United Drug, Inc.

At the present time, debt comprises 56.2% of total capitalization, the 43.8% balance representing Common stock and surplus. After the financing, however, capital structure will be in better balance with 38.8% being represented by debt, 19.4% by Preferred stock and 41.8% by Common stock and surplus.

EARNINGS: Serving a widely diversified territory from Maine to Florida and from New York to California, sales of the Company are primarily determined by the general trend of public purchasing power. This has been increased materially in recent years, with the result that business volume has shown steady annual advances since 1938 to new high record levels in 1942. The following schedule has been prepared from annual reports of the Company, the data being adjusted, however, to give effect to the changes which would have resulted had the new Debentures and Preferred stock been outstanding during the past five years. The wide coverage afforded new interest requirements together with the ample protection available for new Preferred stock dividend needs are well illustrated by the table.

* Assumed rate.

Year	Net Sales	Net Before Charges & Taxes	Total Inc. Taxes**	Revised Net Income ∅	Times Earned / Int. Chgs. Only	Int.& Pfd. Divs.	Pfd. Divs. Only
1942	$121,997,977	$11,408,649	$5,748,000	$3,819,418 #	6.88	3.97	8.04
1941	102,460,960	6,588,479	1,734,690	3,454,250	6.29	3.63	7.23
1940	90,298,132	3,787,030	722,198	1,865,242	3.87	2.24	3.93
1939	89,356,581	3,692,741	587,345	1,896,340	3.92	2.26	3.99
1938	87,867,228	3,015,912	552,487	1,290,738	2.99	1.73	2.72

** At existing rates for various years but increased to give effect to interest saving. ∅ Before reserves for contingencies. / Assuming coupon rate of 5 1/4% and dividend rate of 4 3/4%. These rates have not yet been determined officially. # Before extraordinary charge of $1,160,546 covering modification or cancellation of guaranteed leases.

In connection with the Company's acquisition of the Louis K. Liggett Co. in January, 1934, certain guaranteed long term leases of this subsidiary were assumed. As a result, substantial operating losses were incurred on these leases in each of the following years. In the latter part of 1942, however, the Company paid out and charged against earnings a total of $1,160,546 for the cancellation or modification of certain of such guaranteed leases. These payments and the expiration in June of this year and in April, 1944 of two leases will substantially reduce, henceforth, the annual guaranteed lease loss. The benefit to earnings arising from this action will be evident in 1945 results.

FINANCIAL POSITION: The consolidated balance sheet at May 31, 1943, adjusted to give effect to the financing, indicates that total current assets of $45,525,467 covered aggregate current liabilities of $16,519,641 by around 2.76 times. Net working capital is thus indicated at $29,005,826 or the equivalent of approximately $1,450 for each $1,000 principal amount of Debentures to be outstanding. At the same date, adjusted net tangible assets were equal to around $2,260 per $1,000 Debenture. After deducting the Debentures at par, net working capital was equal to about $90. per share of new Preferred stock and net tangible assets were equal to some $252. per share.

INDENTURE PROVISIONS: Conservative provisions, in our opinion, govern the issuance of additional funded debt and the payment of dividends upon the Company's Common stock. A Sinking Fund totaling $667,000 per year will commence to operate in May, 1944 and is designed to retire $10,005,000 of Debentures, or about 50% of the issue, by maturity.

Charter provisions applying to the Preferred stock, likewise, are conservative, in our opinion. Redemption prices of both issues have not yet been determined but they will be supplied to you promptly as soon as they become available. The new Preferred stock will not have a Sinking Fund.

RECENT DEVELOPMENTS: A major development of the Company's business during recent years has been the coordination and consolidation of its manpower, facilities and operating methods. Additionally, a number of managerial changes have been affected which have greatly increased efficiency. Election of Mr. Justin W. Dart, formerly general manager of Walgreen Co. as president of the Company, is expected, furthermore, to result in substantial improvement in merchandising policies and in overall planning programs for the war and post-war periods. These developments together with change in the Company's policy toward guaranteeing leases should improve materially, in our opinion, its future operating results.

COMPARISON: Attached herewith you will find a comparison of the Company's new Preferred stock with industrial preferred issues of somewhat similar investment characteristics. It will be noted that with only one exception, all of the other issues are quoted at or well above the levels at which they may be redeemed. The ample asset and earnings coverages available for the new issue are well illustrated by the data at the bottom of the table. No similar figures were prepared for the new Debentures, however, because there is only one issue, McKesson & Robbins 5 1/2s due 1956, which is directly comparable with it.

CONCLUSION: There are relatively few good grade industrial bonds available at attractive yields in the present market. Because of this fact as well as the ample protection afforded the new Debentures both as to assets and earnings, the offering, we believe, should be well received. As pointed out above, the new Preferred will, likewise, have many points of appeal and is expected to be offered on better than average yield basis for issues of its class. In our opinion, both issues will be interesting primarily from the standpoint of return together with their conservative appreciation prospects.

July 20, 1943.

HORNBLOWER & WEEKS
E. M. Matalene

A Statistical Comparison Of
Proposed United Drug Company 4 3/4% Preferred Stock
With Other Industrial Preferred Stocks Of Somewhat Similar Investment Quality

Item	United Drug	McKesson & Robbins	Walgreen	Beatrice Creamery	Celanese Corporation	Crane Co.	Glidden	Safeway Stores	United Biscuit	Westvaco Chlorine
Shares Outstanding	100,000	56,000	94,225	91,317	37,710x	192,803	199,540**	214,744	25,000	57,133
Dividend Rate	$4.75	$5.25	$4.50	$4.25	$5.00	$5.00	$2.25	$5.00	$5.00	$4.50
Call Price		109 1/2	106	105 1/2	103	105	52 1/2	110	110	110
Market		113 1/2	108	107 1/4	106 1/4	105 1/2	47 1/2	111 1/2	113 1/2	110
Yield		4.62%	4.16%	3.96%	4.70%	4.74%	4.74%	4.48%	4.40%	4.09%
Capitalization*	**Amount %**	**Amount %**	**Amount %**	**Amount %**	**Amount %**	**Amount %**	**Amount %**	**Amount %**	**Amount %**	**Amount %**
Funded Debt	$20,000 39	$13,816 23	None -	None -	$34,289 35	$8,000 7	$6,000 16	$18,300 23	$6,300 27	None -
Preferred Stock	10,000 19	5,600 9	$9,422 36	$9,132 39	35,071/ 36	19,280 18	9,997 26	21,474 27	2,500 11	$5,713 41
Common & Surplus∅	21,831 42	40,062 68	16,852 64	14,328 61	28,035 29	79,915 75	21,752 58	38,680 50	14,196 62	8,092 59
Total	$51,831 100%	$59,478 100%	$26,274 100%	$23,460 100%	$97,395 100%	$107,195 100%	$37,749 100%	$78,454 100%	$22,996 100%	$13,805 100%
Times Earned-Int. & Pfd. Divs:	**Pfd. Alone / Overall**	**Pfd. Alone / Overall**	**Pfd. Alone / Overall**	**Pfd. Alone / Overall**	**Pfd. Alone / Overall**	**Pfd. Alone / Overall**	**Pfd. Alone / Overall**	**Pfd. Alone / Overall**	**Pfd. Alone / Overall**	**Pfd. Alone / Overall**
1942	8.04 / 3.97	12.86 / 5.40	7.93 / 7.93	4.29 / 4.29	5.13 / 3.18	9.70 / 8.33	4.16 / 3.15	4.21 / 2.89	10.90 / 4.53	4.44 / 4.44
1941	7.23 / 3.63	13.26 / 5.55	7.86 / 7.86	4.82 / 4.82	5.01 / 3.12	8.07 / 6.96	6.40 / 4.67	4.70 / 3.18	8.17 / 3.56	5.04 / 5.04
1940	3.93 / 2.24	13.28 / 5.56	7.43 / 7.43	4.35 / 4.35	4.35 / 2.77	5.54 / 4.83	3.63 / 2.79	4.32 / 2.96	7.86 / 3.45	5.12 / 5.12
1939	3.99 / 2.26	12.43 / 5.24	6.73 / 6.73	5.04 / 5.04	4.33 / 2.76	5.01 / 4.38	3.99 / 3.03	5.76 / 3.81	9.20 / 3.93	4.96 / 4.96
1938	2.72 / 1.73	5.96 / 2.84	4.88 / 4.88	4.18 / 4.18	1.23 / 1.12	0.63 / 0.69	0.25 / 0.49	3.86 / 2.69	8.71 / 3.75	3.13 / 3.13
1937	4.46 / 2.46	9.43 / 4.13	6.50 / 6.50	3.72 / 3.72	2.57 / 1.83	10.37 / 8.89	5.30 / 3.93	2.66 / 1.98	7.91 / 3.46	3.05 / 3.05
1936	6.29 / 3.23	8.76 / 3.88	6.57 / 6.57	4.08 / 4.08	2.54 / 1.81	6.26 / 5.43	6.71 / 4.88	3.31 / 2.36	9.62 / 4.08	2.43 / 2.43
3 Yr. Average	6.40 / 3.28	13.13 / 5.50	7.74 / 7.74	4.49 / 4.49	3.83 / 3.02	7.77 / 6.71	4.73 / 3.54	4.41 / 3.01	8.98 / 3.84	4.87 / 4.87
7 Yr. Average	5.24 / 2.79	10.85 / 4.66	6.84 / 6.84	4.35 / 4.35	3.59 / 2.37	6.51 / 5.64	4.35 / 3.28	4.12 / 2.84	8.91 / 3.82	4.02 / 4.02
Asset Coverages:	**Pfd. Alone / Overall#**	**Pfd. Alone / Overall#**	**Pfd. Alone / Overall**	**Pfd. Alone / Overall**	**Pfd. Alone / Overall#**	**Pfd. Alone / Overall#**	**Pfd.≠ Alone / Overall#**	**Pfd. Alone / Overall#**	**Pfd. Alone / Overall#**	**Pfd. Alone / Overall**
Net Current Assets	$90 / $97	$730 / $277	$164 / $164	$118 / $118	($5) / $48	$220 / $182	$119 / $112	$130 / $116	($78) / ($12)	$65 / $65
Net Tangible Assets	252 / 151	785 / 226	280 / 280	263 / 263	$292 / 135	514 / 385	316 / 236	278 / 196	$317 / $162	242 / 242
Market Equity of Common//	193 / 64	729 / 210	384 / 384	139 / 139	351 / 102	265 / 183	180 / 113	178 / 47	403 / 114	167 / 167

*In thousands ∅Including contingency reserves #Per $100 debt and preferred /Includes $20,253,000 Prior Pfd. and $14,817,900 Second Pfd. x Prior Pfd.
( )-Deficit //Includes equity afforded by market value of any outstanding junior preferred stocks. **$50 par value ≠On basis $100 par stock

EdM:jhc
July 19,1943.

HORNBLOWER & WEEKS
Statistical Department